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# BULLETIN

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**NUMBER 17-B-05  
(Supersedes 16-B-05)**

**TO:** All Licensed Domestic Insurance Companies  
All Licensed Domestic Health Maintenance Organizations  
All Licensed Domestic Health, Medical and Dental Service Companies  
All Authorized Self-Insurers for Workers' Compensation

**SUBJECT:** Reporting Requirements pursuant to North Carolina General Statutes, Part 7, Article 10, Chapter 58 ("Annual Financial Reporting Law")

**DATE:** October 4, 2017

**ATTN:** PRESIDENT OR CHIEF FINANCIAL OFFICER

Bulletin Number 17-B-05, which is effective immediately for financial statements as of December 31, 2017, has been issued to replace Bulletin Number 16-B-05. This Bulletin is intended to communicate certain reporting requirements of the Annual Financial Reporting Law.

The purpose of this General Statute ("GS") is to improve the Commissioner's ability to monitor the financial condition of insurers by requiring (i) an annual audit of financial statements reporting the financial position and the results of operations of insurers by independent certified public accountants, (ii) communication of internal control related matters noted in an audit, and (iii) management's report of internal control over financial reporting. The Annual Financial Reporting Law requirements relate to auditor independence, corporate governance, and internal control over financial reporting.

Every insurer, as defined in GS §58-10-190(8), is subject to the Annual Financial Reporting Law. Insurers having direct premiums written in this State of less than one million dollars (\$1,000,000) in any calendar year and fewer than 1,000 policyholders or certificate holders of direct written policies nationwide at the end of the calendar may request an exemption from the Annual Financial Reporting Law for the year, except that insurers having assumed premiums pursuant to contracts of reinsurance of one million dollars (\$1,000,000) or more will not be exempt.

Terms used in this Bulletin agree with those as defined in GS §58-10-190.

Additionally, there are other reporting requirements throughout the year, as follows:

**Due by October 1, 2017:**

1. Request for Exemption from the Annual Financial Reporting Law [GS §58-10-185(b)]
2. CPA Designation Letter [GS §58-10-205(a) and (c)]
3. Accountant Awareness Letter (“AAL”) [GS §58-10-205(b)]
4. Request for Exemption from the Annual Financial Reporting Law’s Independence of Services [GS §58-10-210(h)]

**Due by November 30, 2017:**

1. Request for Relief from Lead Partner Rotation Requirement [GS §58-10-210(d)]

**Due by May 21, 2018:**

1. Designation of Audit Committee [GS §58-10-195(d), 245(f)]
2. Request for Extension for Filing Annual Audited Financial Report (“AFR”) [GS §58-10-195(b) and (c)]

**Due by June 1, 2018:**

1. AFR [GS §58-10-195(a), 200] **(2 originals)**
2. Accountant’s Letter of Qualifications (“ALQ”) [GS §58-10-235] **(2 originals)**

**Due by August 1, 2018:**

1. Communication of Internal Control Related Matters from the CPA’s (“Internal Control Letter”) [GS §58-10-230] **(2 originals)**
2. Management’s Report of the Insurer’s Internal Control over Financial Reporting (“MRIC”) [GS §58-10-255(a)] **(2 originals)**

**Due dates that fall on weekends or holidays will be due the next business day.**

**These dates are based upon GS §58-10 as referenced above. The above items must be received by the North Carolina Department of Insurance by no later than the due dates specified. Items not received on a timely basis will be considered delinquent and may result in the initiation of actions against the insurer as specified in GS §58-2-70.**

**Notifications and requests to the North Carolina Department of Insurance (the “Department”) Commissioner of Insurance (the “Commissioner”) as specified in this Bulletin are to be addressed to the contact person(s) provided at the end of this Bulletin. It is imperative to use the address provided at the end of this Bulletin for notification to the Commissioner. Failure to do so may result in a delay of the receipt of your filing(s).**

## **Filings due by no later than October 1, 2017**

### **Request for Exemption from the Annual Financial Reporting Law**

Pursuant to GS §58-10-185(b), insurers having direct premiums written in this State of less than one million dollars (\$1,000,000) in any calendar year and fewer than 1,000 policyholders or certificate holders of direct written policies nationwide at the end of the calendar year shall be exempt unless the Commissioner makes a specific finding that compliance is necessary for the Commissioner to carry out statutory responsibilities.

**Requests for exemptions pursuant to GS §58-10-185(b) must be filed with the Commissioner by no later than October 1, 2017.**

### **CPA Designation Letter**

Pursuant to GS §58-10-205(a), each insurer must file a CPA Designation Letter with the Commissioner with the name and address of the independent certified public accountant retained to conduct the annual audit **The CPA Designation Letter must be filed by no later than October 1, 2017.**

### **Accountant's Awareness Letter ("AAL")**

Pursuant to GS §58-10-205(b), each insurer must obtain a letter from the accountant and file a copy with the Commissioner stating that the accountant is aware of the provisions of the insurance laws and regulations of this state that relate to accounting and financial matters and affirming that the accountant will express his or her opinion on the financial statement in terms of its conformity to the statutory accounting practices prescribed by the Commissioner, specifying such exceptions as he or she may believe appropriate. **The AAL must be filed by no later than October 1, 2017. Once the AAL has been filed with the Department, the AAL shall remain in effect until there is a change in CPAs.**

The Department's responsibility regarding the designation of an independent certified public accountant is only to disapprove those not qualified. The Department does not approve the appointment of an accountant.

### **Independence of Services is Required**

Pursuant to GS §58-10-210(g)(1), the Commissioner shall not recognize as a qualified independent certified public accountant or accept an AFR prepared by an accountant who provides to an insurer, contemporaneously with the audit, any of the following non-audit services:

1. Bookkeeping or other services related to the accounting records or financial statements of the insurer.
2. Financial information systems design and implementation.
3. Appraisal or valuation services, fairness opinions, or contribution in kind reports.
4. Actuarially oriented advisory services involving the determination of amounts recorded in the financial statements. The accountant may assist an insurer in understanding the methods, assumptions, and inputs used in the determination of amounts recorded in the financial statement only if it is reasonable to conclude that the services provided will not be subject to audit procedures during an audit of the insurer's financial statements. An accountant's actuary may also issue an actuarial opinion or certification on an insurer's reserves if all of the following conditions have been met:
  - a) Neither the accountant nor the accountant's actuary has performed any management functions or made any management decisions.
  - b) The insurer has competent personnel, or engages a third-party actuary to estimate the reserves for which management takes responsibility.

- c) The accountant's actuary tests the reasonableness of the reserves after the insurer's management has determined the amount of the reserves.
5. Internal audit outsourcing services.
6. Management functions or human resources.
7. Broker or dealer, investment adviser, or investment banking services.
8. Legal services or expert services unrelated to the audit.
9. Any other services that the Commissioner determines, by administrative rule, are impermissible.

Independence is largely predicated by three principles, that the accountant cannot function in the role of management, cannot audit his or her own work, and cannot serve in an advocacy role for the insurer.

#### **Request for Exemption from Independence of Services Requirement**

Pursuant to GS §58-10-210(h), insurers having direct written premium and assumed premiums of less than one hundred million dollars (\$100,000,000) in any calendar year may request an exemption from the Independence of Services requirement referenced in GS §58-10-210(g)(1).

**The insurer must file with the Commissioner a written statement discussing the reasons why the insurer should be exempt from these provisions by no later than October 1, 2017.**

Pursuant to GS §58-10-210(i), a qualified independent certified public accountant who performs the audit may engage in other non-audit services that are not described in GS §58-10-210(g)(1) or that do not conflict with the principles in GS §58-10-210(g)(2), only if the activity is approved in advance by the audit committee.

#### **Filings due by no later than November 30, 2017**

##### **Lead Audit Partner Rotation Requirement**

Pursuant to GS §58-10-210(d)(1) and (2), the lead or coordinating audit partner, having primary responsibility for the audit, may not act in that capacity for more than five consecutive years. The person shall be disqualified from acting in that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five consecutive years. An insurer may apply to the Commissioner for relief from the rotation requirement on the basis of unusual circumstances. **Requests for relief from the partner rotation requirement must be filed with the Commissioner by no later than November 30, 2017.**

GS §58-10-210(d)(1) and (2), should be consulted for additional information required to be submitted to the Department when applying for relief from the partner rotation requirement.

Pursuant to GS §58-10-260(d), the requirements of GS §58-10-210(d) became effective for audits of the year beginning January 1, 2010, and each year thereafter.

#### **Filings due by no later than May 21, 2018**

##### **Designation of an Audit Committee**

Pursuant to GS §58-10-195(d), every insurer required to file an AFR shall designate a group of individuals as constituting its audit committee, as defined in GS §58-10-190(3). The audit committee of an entity that controls an insurer may be deemed to be the insurer's audit committee at the election of the controlling person.

Pursuant to GS §58-10-245(f), to exercise the election of the controlling person to designate the

audit committee, the ultimate controlling person shall provide written notice of the affected insurers to the Commissioner. Notification shall be made timely before the issuance of the statutory audit report and include a description of the basis of election. The election can be changed through notice to the Commissioner by the insurer which shall include a description of the basis for the change. **The election shall remain in effect for perpetuity, until rescinded.**

**Written notification of the designated audit committee must be filed with the Department by no later than May 21, 2018.** If rescinded, written notification of change shall be filed with the Department **no later than 30 days after rescission.**

Refer to GS §58-10-245 for the specific requirements for audit committees.

#### **Request for Extension for Filing Annual Audited Financial Report**

Pursuant to GS §58-10-195(b), extensions of the June 1 AFR filing date may be granted by the Commissioner for 30 day periods upon a showing by the insurer and its accountant of the reasons for requesting an extension and determination by the Commissioner of good cause for an extension. **Requests for an extension of the June 1, 2018, filing date must be received in writing by no later than May 21, 2018.**

If an extension is granted for the filing of an insurer's AFR, a similar extension of 30 days is granted to the filing of the related MRIC pursuant to GS §58-10-195(c)

#### **Filings due by no later than June 1, 2018**

##### **Audited Financial Statements ("AFR")**

Pursuant to GS §58-10-195(a), **each insurer must file with the Commissioner on or before June 1, 2018, two original sets of its AFR.**

Refer to GS §58-10-200 for the required contents of the AFR.

Pursuant to GS §58-10-215, an insurer may make written application to the Commissioner for approval to file consolidated or combined AFRs in lieu of separate AFRs if the insurer is part of a group of insurance companies that utilizes a pooling or one hundred percent (100%) reinsurance agreement that affects the solvency of the insurer and affects the integrity of the insurer's reserves and the insurer cedes all of its direct and assumed business to the pool.

Refer to GS §58-10-215 for specific contents of the required combined or consolidated AFRs.

Pursuant to GS §58-10-220, the audit of the insurer's financial statements shall be conducted in accordance with generally accepted auditing standards. In accordance with AU Section 319 of the Professional Standards of the AICPA, Consideration of Internal Control in a Financial Statement Audit, the independent certified public accountant should obtain an understanding of internal control sufficient to plan the audit.

##### **Accountant's Letter of Qualifications ("ALQ")**

Pursuant to GS §58-10-235, the accountant shall furnish the insurer, in connection with, and for inclusion in, the filing of the annual audited financial report, a letter of qualifications. **Each insurer must file with the Commissioner two original copies of the ALQ for inclusion in the filing of the AFR on or before June 1, 2018.**

## **Filings due by no later than August 1, 2018**

### **Communication of Internal Control Related Matters from the CPAs**

Pursuant to GS §58-10-230(a), each insurer shall furnish the Commissioner with a written communication as to any un-remediated material weaknesses in its internal control over financial reporting noted during the audit. **The Internal Control Letter must be prepared by the accountant within 60 days after the filing of the AFR and two original copies must be filed with the Commissioner by no later than August 1<sup>st</sup>.** If no un-remediated material weaknesses are noted, the communication must so state.

The insurer shall provide a description of remedial actions taken or proposed to correct un-remediated material weaknesses, if the actions are not described in the accountant's communication pursuant to GS §58-10-230(b)

Refer to GS §58-10-230 for the required contents of the Communication of Internal Control Related Matters.

### **Management's Report of the Insurer's Internal Control over Financial Reporting ("MRIC")**

Pursuant to GS §58-10-255, every insurer required to file an AFR pursuant to this Part that has annual direct written and assumed premiums, excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, of five hundred million dollars (\$500,000,000) or more shall prepare a MRIC as defined in GS §58-10-190. **Two original copies of the MRIC as of the December 31 immediately preceding must be filed with the Commissioner along with the communication of internal control matters by no later than August 1<sup>st</sup>.**

Notwithstanding the premium threshold mentioned directly above, the Commissioner may require an insurer to file MRIC if the insurer is in any risk based capital level event, or meets any one or more of the standards of an insurer deemed to be in hazardous financial condition as defined in GS §58-30-60(b).

Refer to GS §58-10-255 to ascertain the form, content, and required supporting documentation of the MRIC and assertions made therein.

Pursuant to GS §58-10-260(f), the requirements of GS §58-10-255, became effective beginning with the reporting period ending December 31, 2010, and remain in effect each year thereafter. An insurer that is not required to file a report because the total written premium is below the threshold and subsequently becomes subject to the reporting requirements will have two years following the year the threshold is exceeded to file a report.

## **Other Filings**

### **Exemptions from Any Part of the Model Audit Rule**

Pursuant to GS §58-10-260(a), upon written application of any insurer, the Commissioner may grant an exemption from compliance with any and all provisions of this Part if the Commissioner finds, upon review of the application, that compliance with this Part would constitute a financial or organizational hardship upon the insurer. **An exemption may be granted at any time and from time to time for a specified period or periods.**

### **Change in CPAs**

Pursuant to GS §58-10-205(c) if an accountant for the immediately preceding filed audited financial report is dismissed or resigns, **the insurer shall within five business days notify the Commissioner of this event.** The insurer shall also furnish the Commissioner with a separate letter within 10 business days after the notification stating whether in the 24 months preceding such event there were any disagreements with the former accountant on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure; which disagreements, if not resolved to the satisfaction of the former accountant, would have caused him or her to make reference to the subject matter of the disagreement in connection with his or her opinion.

The insurer shall also submit a written request to the former accountant to furnish a letter addressed to the insurer stating whether the accountant agrees with the statements contained in the insurer's letter and, if not, stating the reasons for which he or she does not agree; and the insurer shall furnish the response letter from the former accountant to the Commissioner together with its own.

### **Notification of Adverse Financial Condition**

Pursuant to GS §58-10-225, insurers must file with the Commissioner any notification received from their accountant that an adverse financial condition is present. Notification of adverse financial condition **must be filed within five (5) business days of receipt from the accountant** and shall provide the accountant making the report with evidence of the report being furnished to the Commissioner. If the accountant fails to receive the evidence within the required five business day period, the accountant must furnish to the Commissioner a copy of its report within the next five business days.

### **Useful Hyperlinks**

The Annual Financial Reporting Law Bulletin, the NAIC/AICPA Working Group Implementation Guide, and examples of some of the required correspondence have been placed on the NCDOL Website. In order to access these, the NAIC/AICPA Working Group has developed an Implementation Guide. A link to the Implementation Guide has been placed on the NCDOL Website. However, the Annual Financial Reporting Law prevails regarding any discrepancies between it and the NAIC/AICPA Implementation Guide.

1. Go to [www.ncdoi.com](http://www.ncdoi.com)
2. Click on Insurance Industry, drop down to Financial Evaluation
3. Click on Financial Evaluation
4. Click on Financial Examinations
5. Click on Annual Financial Reporting Law
6. Click on Bulletins, or
7. Click on Examples of Correspondence Required

### **Contact Information**

**Please disregard all previous email addresses, telephone numbers, and mailing addresses provided in previously issued CPA Audit Rule Bulletins.** Any questions concerning this Bulletin and all filings required by the Annual Financial Reporting Law should be addressed via the following:

**Email Address:**  
**Direct Telephone**  
**#:**  
**Mailing Address:**

**All Filings, excluding AFR & Internal Control Letters**

**Kait.chase@ncdoi.gov**  
(919) 807-6163

N.C. Department of Insurance  
Attn: Kait Chase  
Agile Enterprise Section  
1203 Mail Service Center  
Raleigh, NC 27699-1203

**AFR & Internal Control Letters**

**SueAnn.webster@ncdoi.gov**  
(919) 807-6612

N.C. Department of Insurance  
Attn: Sue Ann Webster  
Financial Analysis Section  
1203 Mail Service Center  
Raleigh, NC 27699-1203